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MUNICIPAL OWNERSHIP OF PUBLIC UTILITIES *

I am asked for an opinion on the legal aspects of municipal ownership of public utilities in this country—a project presented in a programme fairly definite in its objective, but somewhat vague and discordant as to method.

The programme has been more or less accomplished in certain localities, but is largely in the state of propaganda. This, however, is sufficiently vigorous to warrant serious inquiry as to the pertinent rights and obligations of public authorities, which have received little attention in comparison with economic questions; yet they are vital to investors whenever private undertakings would be affected by the execution of municipal works, important to taxpayers who must contribute to the cost thereof, and of interest to all citizens by reason of the relation of the programme to our institutions.

An "opinion" on a broad subject so slightly developed must lack that pointed application expected in opinions upon concrete cases, but in outlining municipal ownership and considering the relation of law to it we should obtain propositions of general application, and a fair idea of its position and prospects.

MUNICIPAL OWNERSHIP ABROAD.

The business ventures of foreign, and especially of British cities are so frequently cited both in support and in disparagement

* THE JOURNAL takes pleasure in publishing the following opinion prepared in 1907 by Mr. Carman F. Randolph of New York City, which treats an important subject as fully in evidence now as at that time, and of particular consequence in New England. The article will be published in two parts, the second of which will appear in the April number.

of municipal ownership in the United States that it is important to appraise their real bearings.

The most striking value of foreign experiments will come from an accurate estimate of their economic results, which is not within my province; but not less material is an appreciation of their legal environment.

While I shall refer occasionally to foreign law and practice, I shall not give a consecutive and detailed account of municipal ownership legislation abroad,¹ but I venture a few general observations concerning the valuation of foreign experiments from the standpoint of public law.

Whether foreign institutions are better devised than our own for the public management of business enterprises suggests a debate likely to outrun the bounds of useful argument. Civilized communities the world over have too many characteristics in common to warrant the assertion that municipal performances in one country are impracticable in another. Yet between European institutions and customs and ours there are differences not without significance in this relation.

In continental Europe the administrative power of the state, be this a monarchy or a republic, is personified and privileged to a marked degree. Officials great and small compose a civil body approaching the military in the segregation of its personnel from the community at large, and its acts are regulated by a system of administrative law quite distinct from the general system. The result is the subjection of the community to a civil discipline at the hands of a powerful bureaucracy. Bureaucratic government, at its best, promises at least an orderly administration of business enterprises.

In Great Britain there is no such exaltation of administrative power. A ruling House of Commons and a prevailing common law emphasize the subordination of the executive arm.

As yet the United States are, like Great Britain, comparatively free from bureaucracy, though in both countries there are indications of inclination in this direction; and British communities are more akin to ours than are continental cities.

Nevertheless, partly by organization we shall not imitate, partly by habits we cannot borrow, the typical British town seems to come nearer than our own to a business corporation.

¹ I call attention to the elaborate municipal ownership code enacted by the Italian parliament March 29, 1903 (the Giolitti Law). See *Annuaire de Législation Etrangère*, Paris, 1904, p. 207.

Foreign institutions and experiments deserve scrutiny, but we shall have to square our course according to domestic conditions.

BUSINESS AND POLITICAL QUESTIONS.

Popular discussion of municipal ownership is mainly concerned with business and political considerations.

These will not be treated specifically in this legal discussion, though their intimate connection with law will frequently appear, but the main questions should be stated.

The business questions are: First: Whether the community will be better served by public corporations than by private companies?—Whether, giving to the complaints against company service every ounce of their proper weight, it is not generally a more satisfactory service than our average city is likely to render?

Second: Whether the community should venture public funds in these enterprises?

At present the financial risks are borne by individuals and, though the fortunes won by successful ventures are widely advertised, the numerous failures are too often ignored. Probably few intelligent advocates of municipal ownership anticipate a higher average of financial success than companies have attained, yet even an equal percentage of failures would mean widespread disaster to our communities—equaling, perhaps exceeding, the calamitous results that years ago followed municipal adventures in railways.

Coming to political questions, we have to consider the effect of adding to our corps of public servants the employees of gas and electric works and tramways. Nor is this all—a sweeping crusade for municipal ownership might well carry along in its train public operation of railway and telegraph lines and transfer their operatives to the public payroll.

While there is much theoretical and some practical protection against the evil predominance of public servants in politics, weight of numbers and organization would wield an influence beyond legislative control.

A sweeping denunciation of the programme as “socialistic” is a somewhat childish performance in the face of a movement too big and too earnest to be checked by an epithet—which, moreover, is often misused.

The mere public ownership of a tramway which serves a community and occupies its streets is no more socialistic in any con-

troversial sense than the public ownership of a water supply. And when a community operates this tramway upon business principles it is not doing socialistic work.

Scrutiny of municipal ownership abroad by localities does not disclose a uniform connection with the socialist propaganda. Indeed an advanced school of socialists stigmatize it as a bourgeois scheme for community money-getting, and an obstacle to the development of their ideal social state, wherein acquisitive zeal is repressed, if not extinguished.

In Great Britain, where socialism has not been very much in evidence, urban communities covet the anticipated profits of certain undertakings. The shopkeeping instinct seems largely responsible for what is significantly called "municipal trade."

In New Zealand, on the other hand, municipal ownership is one of the normal functions of a state deeply imbued with socialism.

Germany, with millions of socialist voters, is far behind Great Britain in municipal trade.

The socialistic ideas, so highly developed in France, have not greatly promoted municipal ownership. The French people generally prefer to obtain their public services at private risk. Even the socialist town of Roubaix conceded the tramway to an operating company.²

But after all, the programme, however conceived, is more or less socialistic in its tendencies, and a bird's-eye view of its course in Europe features it as a real, though often an unintentional adjunct to the widespread socialist campaign.

American statesmen who would deal wisely with the subject must realize its relation to the larger movement, and they must have more than a bowing acquaintance with the causes, the methods and the aspirations of socialism.

Professor Wagner of Berlin, referring to the leaders of socialist thought in Germany, sagely commends an "unprejudiced and searching criticism" of their doctrines. "Simply to ignore them as was done for so long, is impossible," he says. "It is perfectly consonant with this attitude towards socialism and its scientific spokesmen, and, indeed, it is a plain duty to accept whatever such examination may prove to be right in the criticism and positive teachings of socialism, and to add this to the permanent con-

² P. Mercier: *Les Exploitations Municipales en France*, p. 152.

stituents of scientific political economy. There is much that will stand examination, though by far the greater part cannot. But not less is it imperative upon us to accept in the demands of socialism, and to recognize as worthy of endeavor, such changes and transformations of the economic system of law, even in regard to property and the right of contract, as may be found to be practicable and to be for the public interest. Here, too, something will stand the test, though not, indeed, much. For this question of practicability and expediency the socialists have treated with very irresponsible flippancy; while, true to their arbitrary views of social organization, they have quietly ignored counter-evils altogether; and herein those who hold to the idea of historical development, and entertain social ideals other than theirs, are unable to follow them. Nevertheless, we cannot agree to reject a measure of any kind simply because it happens to emanate from the socialists, or may be termed 'socialistic' by antagonists or the multitude."³

The municipal ownership movement in the United States does not seem to be consciously inspired by socialism to a great degree, or by a deliberate preference for bureaucratic government. It seems to be animated rather by the feeling that company ownership of public utilities is irredeemably sordid and corrupt than by a conviction of the excellence of public management.

On the assumption that companies cannot be properly regulated we are urged to replace them by government agencies.

The truth of this assumption would discredit the remedy. If the voting body has not enough virtue and capacity to regulate the companies it creates is it likely to improve matters by taking over their enterprises? If these qualities are not conspicuous in government by what social chemistry will they shine in commerce?

In truth a municipal project is badly presented unless it accentuates the promise of a service at least equal to company service and at no greater cost, rather than the defects of company management: When defects are remediable by legal process the company would be coerced; when they are beyond reach of reasonable regulation they will persist under municipal management.

THE FUNCTION OF LAW.

The substantial preëminence of political and business considerations does not dwarf the important function of law.

³ *Fortnightly Review*, April, 1907, p. 690.

First, the constructive function. A municipal ownership scheme must be authorized by a legislative act.

This cannot be wisely framed without due regard to the real interests of the community at large and to whatever private interests may happen to be affected.

It is not enough to anticipate that a scheme will pass the constitutional test. It should be conspicuously fair both to the community, whose unchecked zeal might lead to improvidence, and to investors, whose reasonable claims to consideration are not always measured by the constitutional guarantees.

The corrective function of law will be invoked from time to time as the Courts are required to determine a constitutional question, or construe a statute or a contract.

The suitors will not be confined to public service companies intent to protect their interests. Here and there taxpayers will be impelled to test the validity of a scheme threatening to overburden their property. And a city itself may be called upon to assert its claims in Court.

Litigation will be largely conducted in State Courts, and when suits are tried in Federal Courts by reason of the diverse citizenship of the parties State decisions will usually govern. But whenever municipal ownership legislation touches the property of taxpayers or companies it must respect the guarantees of the Federal Constitution, and every suit wherein their benefit is claimed may be carried to the Supreme Court of the United States.

In discussing a programme based wholly upon legislation and containing, perhaps, the germs of a revolutionary propaganda, it is well to emphasize the jurisdiction of American Courts in respect of legislative acts.

The United States are differentiated from, and, to my mind, above all other constitutional governments by a peculiar exaltation of the judicial function which, when performed by an independent bench, is in the long run likely to express more intelligence, fairness and consistency than either the legislative or the executive functions.

In other countries the lawmaking office of the government, be it popular or autocratic, speaks with final authority. Here the legislatures of the Nation and the States are subject to certain constitutional restraints and it is for the Courts to determine, when properly invoked, whether a particular legislative act is or is not

law. Here the law is not simply what the legislature wills, but what it lawfully wills.

When, in 1795, Mr. Justice Paterson of the Supreme Court said, in a District Court opinion:⁴ "Whatever may be the case in other countries, yet in this there can be no doubt that every act of the legislature repugnant to the Constitution is absolutely void," he gave Federal sanction to a power of judicial review which had already been assumed in certain State Courts, and has since become established throughout our country.

GOVERNMENTAL POWER TO ENGAGE IN BUSINESS.

Whether the State shall engage in general business is among the momentous questions of the future—perhaps not far removed from practical discussion.

Thoroughgoing collectivists demand the nationalization of all industries. Socialists of paler type content themselves with advocating public exploitation of great branches of industry which have become more or less concentrated in a few hands.

The American people have been so opposed to government activity in the enterprises within the sphere of private initiative that the question of power has rarely come into Court. In the few decisions the weight of opinion is adverse,⁵ and it is not impaired by State or municipal monopoly of the liquor traffic,⁶ for the fact that this traffic may be entirely prohibited under the police power excludes it from those avocations open to all as of right.

At present we have reason to think that the socialist state would be incompatible with our constitutional system, but we must bear in mind that even organic laws are but writings to be interpreted, and that theories of interpretation are not always inflexible.

In this relation I call attention to efforts of foreign publicists to fit the traditional system of jurisprudence to a socialist state—to preserve through a complete social revolution the continuity of legal form.⁷

Note in the following passage that our Supreme Court, in order to emphasize its forecast of the integrity of Federal revenue in

⁴ *Van Horne's Lessee v. Dorrance*, 2 Dall., 308.

⁵ See *Opinion of the Justices*, 155 Mass., 598; *Hayward v. Red Cliff*, 20 Col., 33; *Opinion of the Justices*, 58 Me., 596.

⁶ See *South Carolina v. United States*, 199 U. S., 437.

⁷ See A. Menger: *L'Etat Socialiste*, Paris, 1904; *Revue Bleue*, May 12, 1906.

all eventualities, contemplates the remote possibility of socialist commonwealths:

"The right of South Carolina to control the sale of liquor by the dispensary system has been sustained. *Vance v. W. A. Vandercook Co.*, No. 1, 170 U. S., 438. The profits from the business in the year 1901, as appears from the findings of fact, were over half a million dollars. Mingling the thought of profit with the necessity of regulation may induce the State to take possession, in like manner, of tobacco, oleomargarine, and other objects of internal revenue tax. If one State finds it thus profitable other States may follow, and the whole body of internal revenue tax be thus stricken down.

"More than this. There is a large and growing movement in the country in favor of the acquisition and management by the public of what are termed public utilities, including not merely therein the supply of gas and water, but also the entire railroad system. Would the State by taking into possession these public utilities lose its republican form of government?

"We may go even a step further. There are some insisting the State shall become the owner of all property and the manager of all business. Of course, this is an extreme view, but its advocates are earnestly contending that thereby the best interests of all citizens will be subserved. If this change should be made in any State, how much would that State contribute to the revenue of the nation? If this extreme action is not to be counted among the probabilities, consider the result of one much less so.

"Suppose a State assumes under its police power the control of all those matters subject to the internal revenue tax and also engages in the business of importing all foreign goods. The same argument which would exempt the sale by a State of liquor, tobacco, etc., from a license tax would exempt the importation of merchandise by a State from import duty. While the State might not prohibit importations as it can the sale of liquor, by private individuals, yet paying no import duty it could undersell all individuals and so monopolize the importation and sale of foreign goods."⁸

MUNICIPAL OWNERSHIP FROM AN INSTITUTIONAL STANDPOINT.

Municipal ownership is, with us, the concern of the States for, outside of our insular territory, the national capital is the only important city under Federal control.

So long as a State maintains the republican form of government required by the Constitution of the United States it is free

⁸ *South Carolina v. United States*, 199 U. S., 454.

to arrange its political system at discretion. Subject to this requirement a State can freely organize and alter its political institutions, and it can invest its public corporations with whatever powers may be exercised without violating Federal rights and guarantees.

So far as State constitutions are concerned the Federal Courts will respect the interpretations of State Courts when Federal questions are not involved.

This rule has been applied in decisions germane to our subject. It has been held, for example, that whether or not a municipal debt limit has been exceeded is a matter of State concern, wherein Federal Courts will follow the adjudication of local tribunals.⁹

This freedom of the States in matters of local policy enables each to decide for itself whether municipal ownership shall be permitted.

The city is the political corporation of immediate interest, and before discussing its relation to the utilities in question we should get an idea of its place in our system of government.

The American city is the creature of the State and is subject generally to its control.¹⁰ The power of the State extends even to the extinction of the corporation—as when a legislature passes “an act to repeal the charters of certain municipal corporations, and to remand the territory and the inhabitants thereof to the government of the State.”¹¹

This power is to be viewed as an essential part of the sovereignty of the commonwealth in all that relates to the governance of its territory. In the absence of a constitutional provision to the contrary there can be no *imperium in imperio*, no sovereign powers of a local character independent of the State.

But our Courts justly hold that the urban community may enjoy property rights which the State is bound to respect. Thus, it may have property which the State can neither freely appropriate, nor divert to other uses.¹²

On the same principle urban taxpayers cannot be compelled to assume whatever burdens the State legislature may choose to impose. A burden may be illegal because it casts upon the community a responsibility of wider concern, or because, while local,

⁹ *Sioux Falls v. Farmers Loan & Trust Co.*, 136 Fed. Rep., 721.

¹⁰ See *Worcester v. Street Railway Co.*, 196 U. S., 548.

¹¹ See *Meriwether v. Garrett*, 102 U. S., 472.

¹² See *Worcester v. Street Railway Co.*, 196 U. S., 537.

it does not involve a duty which the State can compel the community to perform.

Considering the rights of an urban community, it appears that a State cannot compel it to undertake an enterprise not directly connected with some municipal duty.

Applying this proposition to public utility works in general, it would seem that none can be forced upon a city unless the community at large is injured by its neglect—for instance, it is conceivable that municipal shortcomings in the matter of street lighting or water supply might be sufficiently gross to injure the community at large and hence justify State compulsion.

Generally speaking, however, the utilities in question cannot be forced upon a city by the State, and, therefore, should the principle of municipal ownership be an issue in a State campaign, a favorable popular vote, followed by enabling legislation, would not constrain an unwilling community.

The ordinary measure of communal rights is in most States enlarged by constitutional provisions conferring municipal privileges of more or less importance, and each municipal ownership scheme must be scrutinized with regard to these provisions.

THE PROGRAMME.

The municipal ownership movement in the United States does not as yet contemplate the entrance of government into what have been with us always regarded as distinctively private enterprises.

It is mainly concerned with what are called public utility works. These are neither distinctively private nor yet distinctively public. They occupy middle ground and are in a class by themselves with, for the most part, certain common characteristics.

They are under obligation to serve the public, but they are business enterprises, as distinguished from such municipal works as sewers, in these respects: Their services cannot be forced upon individuals; and they are reproductive works, deriving income from the charges collected from all persons who avail themselves of the service.

They are distinguished from ordinary business enterprises by the fact that charges must be reasonable and may be actually regulated by legislation.

Broadly speaking, their business is transportation or transmission as distinguished from the sale of commodities which pass from hand to hand.

Commonly they require a use of public property, usually highways, and when private property is needed it may be expropriated.

They embody the element of monopoly to a greater or less degree. Monopoly is in some cases based upon a legislative act, but usually results from the practical obstacles to useful and profitable competition.

Most of the foregoing characteristics are found in the larger public utilities of which the railroad is the leading type, but there is a marked difference between these and the utilities presented for municipal ownership.

Each acquires a right of way, which is usually but an easement, but the former pay what is practically the full value of the land, while the latter pay comparatively little for their easement when, as is usual, this runs upon or under a highway. When the fee of a highway is in the public they generally pay nothing, except by special contract. When the fee is private it is commonly held that their undertakings impose little or no additional burden.

Waterworks, and gas and electric light plants originated in urban needs and generally retain their urban character. But the tramway, of like origin, has largely outgrown the single town and is rapidly developing a long distance service.

These undertakings may be divided into two classes according as their service is of prime or of secondary importance. In the first class is the water service, for this involves the health and safety of the community. Tramways, telephones and electric power works are in the second class.

The light service has a place in each class. The lighting of city streets is a matter of public concern. The lighting of private houses is not. Yet as a rule it would be improvident to maintain one lighting plant for the public and another for the private use of a community, for public consumption is usually so small in comparison with private that with two services the former would be relatively the more costly. Besides there would be the annoyance of a needless dual use of the streets. Generally speaking either the city or a company must supply all the gas or all the electric light within a given area.

The telephone, originally of urban use, now gives a single service of wide radius and is of both general and local interest.

None of these undertakings is open to citizens as a matter of course, for each, to a greater or less degree, requires a use of public property and an exertion of public powers which citizens

cannot enjoy without the State's permission. And the fact that they require a special franchise for their private exploitation, over and above the franchise required for every corporate undertaking, stamps them as being primarily of State concern. Hence whether they shall be actually owned by public corporations or by private companies is discretionary with the State.

In the absence of a distinct constitutional prohibition the utilities in question are within the competency of public authorities.

Whether the public authority charged with a particular undertaking shall be the State itself, or a city or some other subordinate political corporation depends largely upon the nature and extent of the work.

Whether the public authority shall simply own or shall also operate an undertaking is a question of recurrent interest in this examination, but it must be understood at the outset that, given the right to own property, the question whether the owner shall be lessor or operator is one of expediency.

Municipal ownership of public utilities is in itself no new thing in this country.

Municipal ferries are not unknown, and waterworks are owned by most of the larger and many of the smaller towns.

Municipal control of the water service—most essential and simplest of all urban services—being so widely accepted does not figure in the present discussion, though in adjudications respecting public waterworks we find most of our meager case law in respect of municipal ownership.

The programme in debate commends the municipalization of gas and electric works and tramways, with some disposition to include telephone lines. These complex undertakings are sharply differentiated from waterworks and require us to consider municipal competency in what is, in this country, a comparatively untried field.

Private companies furnish nearly all our gas, and almost, if not quite exclusively, all our tramway and telephone services.

In electric lighting we find that in 1902, 334,000 arc lights were furnished by private companies and 50,000 by public corporations, and of the 18,000,000 incandescent lamps in use public corporations furnished only 1,500,000.¹³

¹³ Census Report on Electric Light and Power Stations, 1902, p. 6.

Our Courts have sustained statutes authorizing cities to supply artificial, and natural gas and electric light.¹⁴

The telephone, and works for the transmission of heat and power are on the same footing, but, as yet, none of these has made much progress in the way of public ownership.

The tramway has fared no better, but New York owns a subway,¹⁵ which, however, is utilized by an operating company.

Municipal ownership of tramways abroad seems to have been facilitated here and there by opportunities for municipal activity in directions almost, if not quite unknown in this country.

When a tramway is projected along a narrow artery in an American town the only way to prevent congestion is to widen the street at a large and sometimes prohibitive cost.

Abroad, however, cities may, in widening streets, expropriate sufficient land to afford suitable building sites on the new frontage and sell the same—the prices being usually enhanced by the improvement of the thoroughfare. The possibilities of thus decreasing the cost of widening are illustrated in the Holborn-Strand improvement in London, where the sale of extra land acquired reduced the gross cost from £7,780,000 to £1,300,000 per mile.¹⁶

In this country, while cities are sometimes required to take and pay for remnants of lots left by widening a street, they do not expropriate and deal in land in the foreign fashion.

The potentialities of tramway service in distributing the population of congested districts are well recognized, and abroad the better housing of the working classes is deemed a lawful subject of public expenditure. Hence foreign cities have undertaken these works together—building houses away from and furnishing transportation to the centers of work.

The possibilities of commercial loss in carrying out a housing scheme are strikingly illustrated in a recent case in London:¹⁷ "In connection with certain street improvements, especially the formation of the new street from Holborn to the Strand now in course of completion, the Council was required, under the author-

¹⁴ *Linn v. Chambersburg*, 160 Pa., 511; *Crawfordsville v. Braden*, 130 Ind., 149; *Hequembourg v. Dunkirk*, 49 Hun, 550; *State v. Toledo*, 48 Ohio St., 212. See also *Opinion of Justices*, 150 Mass., 592.

¹⁵ *Sun Publishing Co. v. New York*, 152 N. Y., 257.

¹⁶ Royal Comm. on London Traffic, I, p. 118.

¹⁷ Royal Comm. on London Traffic, I, p. 10.

izing act, to build workmen's dwellings in place of those that were demolished. For this purpose they bought the Bourne estate, close to the site of the improvement. The cost price was £201,107, being the commercial value. They were obliged to write this sum down to £44,000, its value earmarked for artisans' housing, and to debit the balance to the cost of street improvements. This was necessary in order to admit of charging rents within the means of the families to be provided for. Even after this writing down, they have had to charge rents of from 9s. 6d. to 11s. a week for a three-roomed tenement, in order to reimburse themselves for this artificially-reduced outlay. The buildings erected will accommodate 2,640 persons, and there is therefore a loss of very nearly £60 per head of the persons rehoused, and the whole of this loss falls upon the rates."

In this country a scheme to provide able-bodied persons with homes at the partial expense of the community would seem to be forbidden by our prevalent rule that taxes shall not be levied for a private purpose.

PROCEDURE.

The steps to be taken by a city in order to promote a municipal ownership scheme are too dependent upon particular statutes to be here reviewed in detail. A general review will serve our purpose.

AUTHORIZATION.

State Permission.

While a State cannot, as a rule, compel a city to execute the undertakings in question, a city cannot, unless distinctly authorized by the Constitution, execute them without the State's permission.

This must be evidenced primarily by an act of the legislature, and, as special acts respecting cities are forbidden in most States, it will commonly be a general statute applying to all cities within a defined class.

This statute may grant a complete authorization to any city able and willing to take advantage of it, leaving each one to determine for itself the expediency of undertaking a particular enterprise.

Such liberty of action is not allowed in certain foreign countries wherein each municipal project must be submitted to a superior authority.

In Great Britain, the usual practice is for a municipal corporation to submit its project to an administrative body—as the Board of Trade for tramways, the Local Government Board for gas and water works.

If this body approves, it issues a provisional order which must be confirmed by Parliament before the corporation can act. If the order is uncontested Parliament will usually confirm it as of course; if contested it is treated as a "private act" (what we would call a "special act").

"The object of a private bill," says Sir Courtenay Ilbert,¹⁸ "is in fact to obtain a privilege,—that is to say, an exception from the general law, or a provision for something which cannot be obtained by means of the general law, whether that general law is contained in a statute or is common law. . . . Each bill is considered by a select committee of each House, who hear the promoters and opponents by counsel, consider their private interests, and determine in a quasi-judicial capacity, whether the promoters of the bill have justified their request for a privilege, and whether private interests are properly protected."

In France, the broad and intimate supervision which the State exercises over all the communes from Paris down is manifested in this relation by the rule that projects shall be submitted first to the prefect of the department and finally to the Council of State; and in Italy they must be approved by a royal commission.¹⁹

The foreign practice of submitting each municipal project to a body representing the state is commendable, and there are signs of its adoption in this country.

In New York, for example, cities are now required to submit water supply projects to a State Water Commission.²⁰

Local Approval.

In most States municipal ownership projects must be approved by the local voting body, either by a vote on the project itself or on the debt that would be incurred by its execution.

The requirement is frequently constitutional in form, sometimes distinctly relating to such projects, but more often affecting

¹⁸ Legislative Methods and Forms, 1st ed., pp. 28-29.

¹⁹ See Synopsis of the Municipal Ownership Code, Articles 10-12, *Annuaire de Législation Etrangère*, 1904, p. 210.

²⁰ Laws of N. Y., 1905, c. 723.

them indirectly by way of general provisions in regard to the incurring of indebtedness.

The legislative council of a city is usually authorized to give official local sanction to a municipal ownership scheme, but it is not necessarily the depository of power.

A recent decision is of interest in this relation. The New York legislature transferred the power to grant franchises from the Board of Aldermen to the Board of Estimate and Apportionment, consisting of the mayor, the borough presidents and the comptroller. The aldermen contested the validity of the statute, contending that they were exclusively vested with the control of the streets, and therefore the sole authority contemplated by the Constitution for the granting of franchises. The Court of Appeals held that the legislature could thus transfer the control of streets from one body to another.²¹

BORROWING POWERS.

Rarely will a city be able to build or buy a public utility work without borrowing money. Even with a reasonable prospect that the income will ultimately recoup the cost, funds must be obtained immediately, and these must be borrowed for they will far exceed the taxpayers' ability to pay outright. The burden must be distributed.

The connection between the municipal ownership programme and public debts is a vital one. I say "public" and not "municipal" debts to emphasize what is too often ignored—the substantial interrelation of all the local and the general obligations of a State from the standpoint of the public credit.

Debts commonly require the imposition of taxes for their liquidation, and we must anticipate a heavy increase if these municipal ventures multiply.

Now, with increasing local taxes urban communities are less inclined and less able to bear their proper share of general burdens and when this condition is widespread the community at large is seriously prejudiced. Hence the interest of the State in local borrowings. Hence its intense concern in the huge borrowings involved in a considerable exploitation of the municipal ownership programme.

State regulation of municipal borrowing is a marked feature of public finance in Europe.

²¹ *Wilcox v. McClellan*, 185 N. Y., 9.

Excepting so far as the corporation of the city of London has a general statutory power to borrow for certain purposes, British cities can borrow for their business enterprises only to the amounts and on the terms prescribed by the central authority; and the borrowings of French and Italian cities are also supervised by the state.

An interesting feature of the English system is the provision for loaning national funds to local authorities for certain purposes and on easy terms. Under the Public Works Loans Act the Local Government Board has thus lent large sums of money.²²

Debt Prohibitions and Limitations.

In this country most States express by constitutional provisions their concern in municipal debts. First in order is a provision that no city shall pledge its credit without the consent of the voting body. This assures the direct consent of the community to the initial expenditure on account of a public utility work.

Also, there are provisions imposing limits on municipal indebtedness in general, usually a certain percentage of the value of the taxable property.

Besides the foregoing general provisions, we find in certain constitutions special provisions of interest.

In two memorable periods certain States and communities adventured heavy sums in transportation enterprises. The whole story of these earlier ventures is full of instruction; but here the briefest note must suffice, for I am concerned only with their influence on our laws.

When railroads were novelties the idea of State ownership captivated many communities where private capital was inadequate to meet the popular demand for them, and there was also a large pledging of State credit in aid of privately owned lines.

Precedents of a sort were not lacking in the earlier ventures in public canals. But the difference between digging a waterway and running a railroad was soon manifested. With some exceptions the results ranged from embarrassment to disaster. Indeed, railroad ventures contributed to that repudiation of debt which has left its stigma on several States. Influenced by these experiences, certain commonwealths, including Michigan, Wisconsin, Iowa, and Kansas, enacted constitutional provisions forbid-

²² See Redlich and Hirst, "Local Government in England," I, 392; II, 290.

ding the State to engage in or lend its credit to works of internal improvement.

Disastrous ventures with State funds failed to impress their broad lesson upon our people. Many cities pledged their credit in aid of private railroad projects, and the Courts, with few exceptions, sustained the constitutionality of the enabling statutes.

Again misfortune led several commonwealths to raise constitutional barriers against future improvidence—provisions were enacted forbidding such pledgings of municipal credit.

Decisions interpreting these constitutional provisions and kindred statutes make a long and intricate chapter of the law of municipal bonds. A substantial development of the municipal ownership programme is likely to add to its length and complexity, but at present we are concerned simply with the general effect of these provisions.

Do prohibitions against a State's undertaking or aiding internal improvement works extend to cities? In Michigan the Courts hold that cities may be authorized to undertake gas and electric light works, because these minister to the performance of a public duty and so are not included in "internal improvements"; but, rightly placing a tramway in this category, they hold a city incompetent to undertake it on the broad ground that a prohibition designed to guard the community at large from a dreaded form of extravagance must apply to its local divisions.²³

Provisions forbidding cities to pledge their credit in aid of railways have not as yet been much discussed in relation to municipal ownership, but it has been held in New York that this prohibition does not bar the legislature from authorizing a city to issue bonds for constructing a local railway on its own account.²⁴

In case a city is unable to pledge its credit to obtain funds for a particular undertaking because the cost would exceed its debt limit, is it barred from raising funds by way of a mortgage upon the undertaking?

This question was lately presented in a peculiar way. With the hope of enabling Chicago to acquire the street railways in despite of the debt limit, the Illinois legislature passed the "Mueller Law,"²⁵ authorizing the city to raise the necessary pur-

²³ *Atty. Gen. v. Pingree*, 120 Mich., 550: compare cases cited in Cooley's *Constitutional Limitations* *216.

²⁴ *Sun Publishing Co. v. New York*, 152 N. Y., 267.

²⁵ Laws of 1903, p. 285.

chase money by issuing and selling "street railway certificates" to the amount of \$75,000,000. The statute made these certificates a mortgage on the property acquired and expressly stated that they involved no pledge of the city credit. In case of default the purchaser at foreclosure sale should be entitled to operate the railways for twenty years.

The Supreme Court of Illinois has declared the Mueller Law unconstitutional.²⁶ It holds that the mortgage is "something more than a purchase money mortgage; that the purchaser at a foreclosure sale . . . would secure nothing of value as a street railway unless he acquired the right to operate the street railway which he purchased in the streets of the city, and that such right in no way represents any part of the money derived from the issue and sale of said street railway certificates." The Court concludes that, despite the terms of the act, the sale of the certificates and the execution of the mortgage would, by reason of the pledge of substantial rights in the streets, create a debt of the city; and this, added to its present debt, would exceed the constitutional maximum.

Had the Mueller Law been sustained in Illinois upon a principle generally approved, many cities would, in point of law, be authorized to embark in commercial enterprises without regard to their present indebtedness, but the decision rendered should tend to discourage similar attempts to circumvent debt limits.

It has recently been decided that where the jurisdiction of a public water supply corporation includes a town, the town cannot object that its share of the cost will exceed its debt limit. The limitation is imposed on the town only and does not affect the district covered by the larger corporation.²⁷

The practical effect of this decision is to impose upon the town a debt which the town authorities could not lay.

If, as I point out later, it is likely that certain undertakings now assumed to be within the competency of single towns shall really call for public corporations of wider jurisdiction, the application of the rule in the Kennebec case might frequently enlarge the gross indebtedness of communities which, as municipal corporations, had reached the limit.

²⁶ *Lobdell v. Chicago*, 81 N. E. Rep., 354, 362.

²⁷ *Kennebec Water District v. Waterville*, 96 Me., 234.

MUNICIPAL OPERATION.

Whether a city which owns an undertaking shall operate it or lease it to an operating company is a question of vital interest.

Whether municipal ownership shall be passive or active, divides even the advocates of the programme, and apprehension of public operation arrays against the entire programme many who would not object to mere public ownership of all the utilities. The reason is plain: As lessor the city has simply to make and enforce a contract; as operator it must manage a business.

Premising that municipal competency to maintain pipes for distributing water and collect compensation from consumers by no means suggests an equal competency in managing gas and electric works, telephones and tramways, let us consider some of the salient points suggested by municipal operation of these complex utilities.

Administrative Control.

The first administrative requisite is a board of control so constituted as to afford the largest scope for sound business management and the least for partisan activity—in short, a board approximating the best type of business management as nearly as political conditions will permit. I say “approximating” because the best public board is not likely to match the most efficient private administration.

In this relation it is interesting to note that a few of our urban communities have discarded the traditional mayor and council and have vested local government wholly or partially in commissions of extraordinary organization and power.

Galveston, for example, is now governed by a small group of men each elected by the community at large, each immediately responsible for a particular branch of government and together responsible for the entire governance of the town.

Other towns are trying commission government on a less extensive scale. The small city of Baton Rouge, Louisiana, has lately been authorized to organize as its board of public works “a permanent syndicate of citizens” comprising seven members. Of these the presidents of three local banks are *ex officio* members; the rest are to be citizens at large of approved business capacity, two of whom are to be selected at once by the council for one and two-year terms respectively. The five members

then select two other citizens. The board is self-perpetuating. The members serve without pay. Acceptance of an elective city office is equivalent to resignation. The board has exclusive charge of all public works, awards the contracts and receives and appropriates the necessary funds.²⁸

The commission system seems to have been adopted in the hope of improving local government generally by concentrating personal responsibility, and not with special intent to equip a town for operating public utilities; but it would seem to be better devised than the prevailing government for the management of business enterprises.

Employees.

In regard to employees we have to consider how far their selection and the conditions of their employment may be subjected to a peculiar regulation by reason of the undertaking being a public, and not a private work.

While the preference of a community for employing its own members may perhaps be somewhat promoted by legislation, it cannot be made a positive obligation.

A rule discriminating against citizens of other States, for example, would violate the Federal Constitution which says, "the citizens of each State shall be entitled to all privileges and immunities of citizens in the several States."

Whatever advantages trades unions may hope to obtain from municipal operation, it must be clearly understood that in the matter of employment the unionist as such cannot obtain a direct preference in law. Public authorities must maintain an "open shop."²⁹

This obligation is too deeply rooted in the equality of all men before the State to be squarely impugned.

The State can, however, restrict certain employments to persons whose qualifications have been certified by a public board of examiners.

This practice is most broadly illustrated in a general civil service system which scientific advocates of municipal operations commend as being essential to sound administration. Yet we

²⁸ Laws of La., 1904, c. 171.

²⁹ See *Fiske v. People*, 188 Ill., 206; *Marshall v. Nashville*, 109 Tenn., 495; *Lewin v. Board of Education*, 102 N. W., 756.

are by no means assured that this would prevail in the generality of towns.

Besides civil service rules, which pertain exclusively to governmental service, there are laws of general interest requiring persons seeking certain employments to present official certificates of technical competency.

These laws are based on the police power, and are relieved from the stigma of illegal class legislation only when the employment is a proper subject for regulation in the interests of health and safety, and the requirements are no greater than these interests demand.³⁰

A very substantial proportion of public service employees seems to be within the class amenable to certificate legislation, *e.g.*, engineers, motormen, gas-fitters, persons employed in electric wiring, etc.

What attempts might be made by trade unions to monopolize such employments through ingenious certificate laws, and how far they would succeed, are interesting questions.

Legislation regulating the working hours and wages of persons employed by a public authority is broadly valid on principle, when it merely defines the position which every employer assumes in proffering the terms of employment. Here the statute or ordinance is but the public equivalent of a private offer.

But a question of great interest in connection with municipal operation is whether or how far a State legislature can lawfully determine for a city the hours and wages of its business employees—whether, conceding for the sake of argument the State's right to so legislate for municipal employees in purely governmental service, it has an equal power in respect of those employed in business enterprises.

Now, when the State is competent to fix the hours for private employment in the interests of health and safety,³¹ it is, of course, competent to do the like for municipal employment, and it has been held that the legislature may go so far as to require cities to pay at least the wages prevailing in the vicinity for like employment.³²

The Supreme Court holds that a Kansas act requiring contractors on public works to observe an eight hour day and pay at least

³⁰ *People v. Warden*, 144 N. Y., 629.

³¹ See *Holden v. Hardy*, 169 U. S., 366.

³² *Ryan v. New York*, 177 N. Y., 271.

the wages current in the locality is not repugnant to the guarantees of the Federal Constitution—"it belongs to the State," says the Court, "as the guardian and trustee for its people, and having control of its affairs, to prescribe the conditions upon which it will permit public work to be done on its behalf, or on behalf of its municipalities."³³

Whether labor laws be radical or conservative, there is danger that the political influence of a great corps of public employees will be seriously abused; yet their disfranchisement during the term of service, which has been advocated abroad as the only way to avoid a tyrannous pressure, is not likely to be seriously urged here. It is even problematical how far legislation could be enacted and enforced to prevent improper combinations to raise wages, reduce hours, etc.

Materials and Supplies.

While a State and its subordinate corporations generally buy the things they need, there is no legal objection to their producing anything required for their service, from battleships to red tape.

A city operating a given undertaking may be authorized to manufacture everything required for its prosecution.

Furthermore it can dispose of property no longer needed, and sell by-products, such as coal-tar and coke. A city owning water-works can lease the water power.³⁴ These practices do not denote a general trading activity. They simply mean that a corporation is not obliged to be improvident because it is public.

In Great Britain certain towns which manufacture articles for their own use—plumbers' fittings, for instance—regularly sell them in the market, but the practice would seem to be unlawful in this country, unless, perhaps, the economical construction and operation of a plant should require production beyond the city's needs—a *bona fide* surplus.

Usually a city will purchase and not produce materials and supplies and, despite the notion that the transfer of utilities from private to public management will somehow divorce them from selfish commercial interests, it will be fortunate indeed if its transactions shall be free from "graft".

³³ *Atkin v. Kansas*, 191 U. S., 222; See also *Ellis v. United States*, U. S. Supreme Court, May 13, 1907. Compare *People v. Grout*, 179 N. Y., 417.

³⁴ *Pikes Peak Power Co. v. Colorado Springs*, 105 Fed. Rep., 1.

Possibilities of graft apart, we have to consider the action of the average municipal corporation in regard to the steady and at times the extraordinary expenditure required for the proper maintenance of an undertaking.

A well managed public service company buys supplies in the best market, but this market is not so fully assured to the city.

Doubtless foreign markets cannot be cut off by the action of a State, and, be it noted, the Supreme Court rejected the impudent contention that a municipal ordinance selecting Trinidad asphalt, there being domestic asphalt in the market, was an unlawful regulation of Federal commerce.³⁵

In regard to domestic markets it is settled that one State cannot directly discriminate against the products of another, but there is a difference of opinion on an interesting point. The Supreme Court of Missouri has upheld a city contract prescribing that all the stone required for a particular work shall be dressed in the State, it being expected that the high freight charges for bringing in stone in the rough would practically compel recourse to the local product.³⁶ The New York Court of Appeals declares such a regulation violative of the Federal power to regulate commerce.³⁷ The Supreme Court will some day decide the question. Yet, however wide the market formally assured by constitutional law, local pride and self-interest will constantly and ingeniously work to the preference of local markets.

Fiscal Management.

Advocates of municipal operation differ as to the controlling principle of fiscal management.

A radical administration will press for cheap service even at the cost of saddling annual deficits on the taxpayers, but at present there is little disposition to call upon A to help pay B's gas bill and car fare.

A conservative administration will endeavor so to regulate service charges as to make the enterprise at least self-supporting.

One type, however, will seek substantial profits, either to provide funds for other enterprises or directly to reduce taxes. The first objective is likely to beget improvident expenditures. The second discloses a tendency, if not a purpose, to replace taxes by

³⁵ *Field v. Barber Asphalt Co.*, 194 U. S., 622.

³⁶ *Allan v. Labsap*, 188 Mo., 692.

³⁷ *People v. Coler*, 166 N. Y., 144.

commercial profits. This purpose has been said to underlie public ownership projects in Italy—the government reaching out for a commercial income because of the difficulties in tax-gathering.³⁸

The other, and the better type, seeks no profit beyond the sums necessary to improve and, if possible, cheapen the service. When a city aims only to make a business enterprise self-supporting the charges will be as low as is consistent with proper service, and the enterprise is more likely to be managed with a single regard to its own interests.

This last consideration is of the very first importance, for unless each enterprise be treated as an independent unit its true financial condition is likely to be obscured.

STATE SUPERVISION.

The State, having authorized a city to embark on a business enterprise, has a right to supervise the conduct of it.

I shall not consider the extent of supervision, but it must be insisted that the State should prescribe a general system of accounting and provide for an audit by persons quite independent of the city government.

If it be objected that the surveillance of outside auditors is contrary to the principle of home rule, the quick answer is that when the State authorizes a city to manage a complicated business it is entitled to be apprised of its conduct.

The imperative necessity of a thorough and impartial audit is demonstrated by English experience,³⁹ and I quote liberally from a report on municipal trading made by a joint select committee of Parliament:⁴⁰

6. The first branch of the subject with which the Committee decided to deal was that of municipal accounts, with regard to the form in which they are prepared, the systems under which they are audited, and the right of access to them possessed by the rate-payers. The evidence taken has been mainly directed to these questions.

³⁸ See Lucien Petit: *L'Extension du Domaine Industriel des Communes*, *Revue Politique et Parlementaire*, Jan. 10, 1906, p. 48.

³⁹ See *Attorney General v. De Winton*, 1906, 2 Ch. D., 119; *Law Times*, July 21, 1906.

⁴⁰ Blue Book 270, 1903, page v.

7. Whatever view may be taken of the proper limits, if any, which can be set to municipal trading, it is clearly important that wherever it exists, ratepayers should not be less fully and continuously informed of the success or failure of each undertaking than if they were shareholders in an ordinary trading company.

8. In a large number of cases this is undoubtedly done. But there is in some instances evidence to a contrary effect, and in view of the ever-increasing number and magnitude of municipal undertakings, it is most desirable that a high and uniform standard of account-keeping should prevail throughout the country.

9. The Committee are doubtful whether it would be possible to prescribe a standard form of keeping accounts for all municipal or other local authorities, having regard to the varying conditions existing in different districts. But they recommend that the Local Government Departments should invite the Institute of Chartered Accountants, the Incorporated Society of Accountants and Auditors, and the Institute of Municipal Treasurers and Accounters of England and Wales, and the Society of Accountants in Edinburgh, and the Scottish Institute of Accountants, Glasgow, to confer and report upon the matter.

11. The Committee recommend that a uniform system of audit should be applied to all the major local authorities, viz.: the Councils of counties, cities, towns, burghs, and of urban districts.

12. At present Municipal Corporations in England and Wales, with a few exceptions, are only subject as regards audit to the provisions of the Municipal Corporations Act, 1882, by which one auditor, who must be a member of the Town Council, is nominated by the Mayor, and two, who cannot be members of the Town Council, are elected by the ratepayers.

13. The evidence shows that no effective system of audit is thus supplied. The elective auditors are poorly paid, or are unpaid altogether, little interest is taken in their election, and although in some cases they are able to lay a finger on a particular irregularity, it is not clear that they could not make the same discovery in the capacity of active ratepayers. No complete or continuous audit is ever attempted by them.

14. All County Councils, the London Borough Councils, and Urban District Councils, are subject to the Local Government Board audit. This audit is carried out by District Auditors, who as a rule are not accountants, and are not, in the opinion of the Committee, properly qualified to discharge the duties which should devolve upon them. By special local acts the Corporations of Tunbridge Wells, Bournemouth, and Southend-on-Sea must, and the Corporation of Folkestone may, adopt the Local Government Board system of audit. The duties of the auditors seem to be practically confined to certification of figures, and to the noting of illegal items of expenditure.

15. To apply this system of audit to Municipal Corporations would arouse strenuous opposition from them, and the course may be considered impracticable; but in addition to this, the fact that district auditors are not accountants seems to unfit them as a class for the continuous and complicated task of auditing the accounts of what are really great commercial businesses.

16. The Committee accordingly recommend that—

(a) The existing systems of audit applicable to corporations, county councils, and urban district councils in England and Wales, be abolished.

(b) Auditors, being members of the Institute of Chartered Accountants or of the Incorporated Society of Accountants and Auditors, should be appointed by the three classes of local authorities just mentioned.

(c) In every case the appointment should be subject to the approval of the Local Government Board, after hearing any objections made by ratepayers, and the auditor, who should hold office for a term not exceeding five years, should be eligible for re-appointment and should not be dismissed by the local authority without the sanction of the Board.

(d) In the event of any disagreement between the local authority and the auditor as to his remuneration, the Local Government Board should have power to determine the matter.

(e) The Scots' practice of appointing auditors from a distance in preference to local men, to audit the accounts of small burghs should in similar cases be adopted in England.

17. The Committee are of opinion that it should be made clear by statute or regulation that the duties of those entrusted with the audit of local accounts are not confined to mere certification of figures. They therefore further recommend that—

(a) The auditor should have the right of access to all such papers, books, accounts, vouchers, sanctions for loans, and so forth, as are necessary for his examination and certificate.

(b) He should be entitled to require from officers of the Authority such information and explanation as may be necessary for the performance of his duties.

(c) He should certify—

(i) that he has found the accounts in order or otherwise, as the case may be;

(ii) that separate accounts of all trading undertakings have been kept, and that every charge which each ought to bear has been duly debited;

(iii) that in his opinion the accounts issued present a true and correct view of the transactions and results of trading (if any) for the period under investigation;

(iv) that due provision has been made out of Revenue for the repayment of Loans, that all items of receipts and expenditure and all known liabilities have been brought into account, and that the value of all assets has in all cases been fairly stated.

18. Auditors should be required to express an opinion upon the necessity of reserve funds, of amounts set aside to meet depreciation and obsolescence of plant in addition to the statutory sinking funds, and of the adequacy of such amounts.

19. The Auditor should also be required to present a report to the Local Authority. Such report should include observations upon any matters as to which he has not been satisfied, or which in his judgment called for special notice, particularly with regard to the value of any assets taken into account.

25. With a continuous, vigilant, and thoroughly efficient system of inspection and audit, the surest guarantee to the rate-payers against extravagance is to be found in the deterrent effect of public exposure, in addition to the existing legal remedies.

The best municipal administration of a complex utility work is likely to suffer by comparison with the best private administration; for, being a part of the great machine of government, it will rarely display the freedom of action, the singleness of purpose and the enterprising spirit of the private company.

Flexible powers in raising and spending public moneys are generally denied as being incompatible with honest and prudent administration. Maintenance of this rule will frequently check the development and embarrass the conduct of a municipal business. Its relaxation would open the door to waste and corruption.

A French publicist clearly states the dilemma: "To leave on the one hand the flexibility of action which a business enterprise needs; to maintain on the other the strict control which a municipalized business demands: Here is the almost insurmountable obstacle of every municipalization law. It is the union of these two contradictory conditions which makes the administrative problem of municipalization difficult, and yet they are inevitably fixed by the mere conjunction of the two words: *business* and *town council*. The primary condition of existence of a business enterprise is really freedom of movement; the imperative need of communal life is guardianship and dominant control."⁴¹

(To be continued)

⁴¹ Pierre Mercier: *Les Exploitations Municipales en France*, p. 262.